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Te Pātaka Rangahau a Te Whare Pāremata

MONTHLY ECONOMIC REVIEW






October 2014

(Latest data as at 8 October)

Parliamentary Library Research Paper

A Overview

Recent trend

	2012/13	2013/14	
 Economic Growth	2.2%	3.5%	Annual average GDP Growth (June year)
 Unemployment	6.4%	5.6%	Unemployment Rate (June quarter)
 Inflation	0.7%	1.6%	Annual Inflation Rate (June year)
 Current Account Deficit	\$7.9b	\$5.8b	Current Account Deficit (June year)
 Interest Rates	2.65%	3.71%	90 Day Bank Bills (September month)

Latest data and events

The economy grew by 0.7 percent in the June 2014 quarter, with an expansion in business services influencing growth. There was strong growth for both administrative and support services; and professional, scientific, and technical services over the quarter. Household consumption increased by 1.3 percent over the quarter, due to increased spending on durable goods (e.g. whiteware) and services. On an annual average basis, the economy expanded by 3.5 percent over the year ended June 2014.

New Zealand's current account deficit totalled \$5,798 million in the year ended June 2014, equivalent to 2.5 percent of gross domestic product (GDP). This compared with a deficit of \$7,893 million in the June 2013 year (3.7 percent of GDP). The improvement in the deficit was driven by an increase in the goods balance, which was partially offset by a rise in foreign investor earnings on their New Zealand investments.

Fonterra announced that it was reducing its forecast payout for the 2014/15 season to \$5.30 per kilogram of milksolids (kg/MS), down 70 cents from its previous forecast (excluding dividends). This compares with a payout in the 2013/14 season of \$8.40 per kg/MS. Strong international milk production, Russia's ban on dairy product imports from a number of countries, and high inventory levels in China were believed to be significant factors behind the current fall in international dairy product prices. Since the announcement, international dairy prices have fallen further.

The Reserve Bank issued a statement in late September in which it noted that the New Zealand exchange rate is "*unjustified and unsustainable*". Figures released later that month showed the Bank had sold a net \$521 million into currency markets during the month of August.

Outlook

Annual economic growth may have peaked, with *NZIER Consensus Forecasts* expecting economic growth of 3.3 percent for the year ended March 2015 (although the Reserve Bank has the economy expanding by 3.6 percent). Fonterra will be watching international dairy auction results closely, as their latest payout forecast is based upon a lift in dairy prices from current levels. Survey results are consistent with further employment growth, albeit at a more moderate pace. The Reserve Bank is expected to keep the official cash rate on hold for the remainder of 2014 (at least), while further intervention in the foreign exchange market is a possibility.

Topic of the month: New Zealand Income Survey

B Economic Growth

Background

A country's gross domestic product (GDP) is a measure of economic activity during a set period of time, normally reported on a quarterly and an annual basis. It is the sum of money values of all final goods and services produced in an economy over a set period. The primary indicator used for tracking economic performance over time is known as real gross domestic product, or real GDP. Real GDP is gross domestic product adjusted for changes in prices. New Zealand's official gross domestic product figures are sourced from Statistics New Zealand.

Gross domestic product

New Zealand's gross domestic product has grown in real terms in every quarter since the start of 2011. In the June 2014 quarter, GDP expanded by 0.7 percent, driven by a 4.2 percent rise in the business services sector. Retail trade and accommodation increased by 1.4 percent, while construction activity grew 2.2 percent. Agriculture, forestry and fishing was down 2.8 percent, partially offsetting other growth.

Expenditure GDP rose 0.5 percent in the quarter. Exports of goods fell by 3.4 percent partially due to a fall in meat products and other foods, beverages and tobacco. Imports increased by 2.9 percent with imports of capital goods up 11 percent. Inventories increased by \$650 million in the quarter.

On an annual average basis, the economy expanded by 3.5 percent, the highest annual rate recorded since the year ended September 2007.

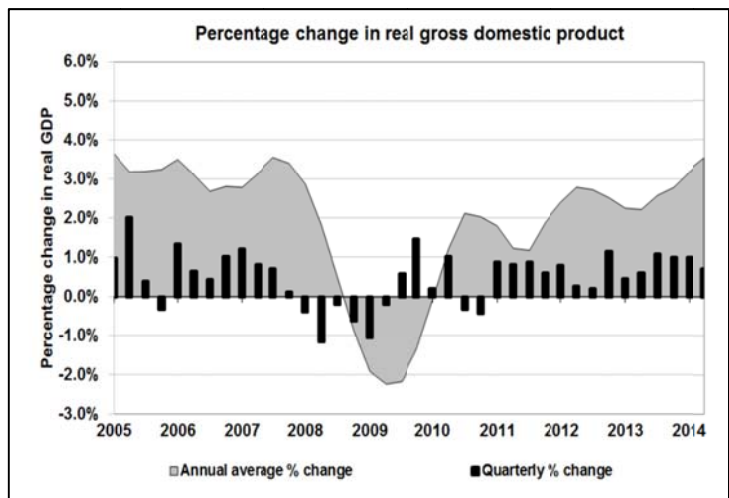
Other data

The fall in global dairy prices has continued with prices in the latest auction falling 7.3 percent. Fonterra has reduced its forecast payout for the 2014/15 season to \$5.30 kg/MS and bank economists are forecasting this to fall further with ANZ forecasting a payout of \$4.85 kg/MS and Westpac forecasting \$4.80 kg/MS. The reduced milk payout is likely to have a negative impact on the wider economy.

Statistics New Zealand figures for August show that while the trend for the number of new dwellings consented is at its highest level since August 2007, the rate of growth is slowing. Auckland and Canterbury comprised almost 60 percent of new dwellings consented.

Outlook

According to Treasury's 2014 *Pre-election Economic and Fiscal Update*, on an annual average basis, economic growth is forecast to peak at 3.9 percent in the 2014 calendar year before easing to 2.1 percent in 2017. The NZIER's *Quarterly Predictions* for September 2014 forecasts growth of 3.6 percent in the year to March 2015 lowering to 2.6 percent in the year to March 2016.



Year ended June 2014	Nominal GDP
Expenditure GDP	\$229,146 million
GDP per capita	\$51,187

Source: Statistics New Zealand.

ANZ Business Outlook Survey	Aug-14	Sep-14
Net % expecting an improvement in business conditions in 12 months' time	24.4	13.4
Net % expecting an improvement in their own firm's activity in 12 months' time	36.6	37.0

Source: ANZ Bank, Business Outlook survey.

GDP growth (%)	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14
Annual (year-on-year)	2.2	2.6	2.8	3.2	3.5
Quarterly (seasonally adjusted)	0.6	1.1	1.0	1.0	0.7

Source: Statistics New Zealand.

Next Release: Gross Domestic Product: September 2014 quarter.

Date: 18 December 2014

Background

The unemployment rate measures the number of people unemployed as a proportion of those in the labour force. The labour force is the number of people of working age (15 years and over) who are working for wages or a salary, working for a family business, or who are unemployed and seeking work. In New Zealand, the official unemployment rate is sourced from Statistics New Zealand's quarterly Household Labour Force Survey.

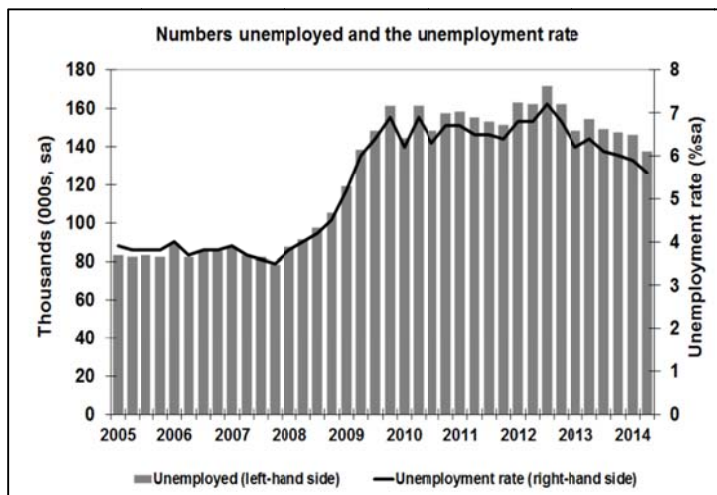
Employment and unemployment

New Zealand's unemployment rate fell to 5.6 percent in the June quarter (seasonally adjusted), its lowest level in over five years. In the Canterbury region unemployment was 2.8 percent in the quarter with construction and retail trade, accommodation and food services leading employment growth.

For New Zealand as a whole, people employed in the construction industry increased 29,600 over the year to June 2014, up 16.8 percent, while those employed in the wholesale trade sector grew 20.3 percent (up 16,800). In contrast, the number of people employed in the agriculture, forestry and fishing sector fell by 5.8 percent over the year.

The number of Pacific peoples employed rose by 18,000 (19.3 percent) in the year to June 2014. This was the largest annual movement since the series began in December 2007.

Actual and usual hours worked also grew over the year up 4.8 percent and five percent respectively with a small increase in the quarter to June 2014 (up 0.3 percent and 0.6 percent respectively). The annual growth in actual hours worked was higher than employment growth leading to an increase in average hours worked.



Other data

The ANZ Bank's job advertisements index has flattened over the last few months after a higher level of activity at the beginning of the year. According to the Ministry of Business, Innovation and Employment, skilled job vacancies advertised online grew by 1.7 percent in August with an 11.6 percent increase in the past year. The *Westpac McDermott Miller Employment Confidence Index* continued to rise in the September quarter and is now at its highest level since September 2008 although still well below pre-recession levels.

Outlook

The Reserve Bank *Monetary Policy Statement* for September 2014, forecasts an unemployment rate of 5.1 percent for the year to March 2015, remaining around that rate until 2017. Employment growth over the year to March 2015 is forecast at 2.3 percent, lowering to 1.1 percent by March 2017. The NZIER's *Quarterly Predictions* for September 2014 forecast employment growth of 2.4 percent in the years to March 2015 and 2016 with a decrease in employment of 0.9 percent in the year to March 2017.

ANZ Business Outlook Survey	Aug-14	Sep-14
Net % expecting to increase employment in their business in 12 months*	18.0	21.3
Net % expecting the unemployment rate to rise in 12 months*	-24.7	-16.8

*equal to the % of respondents expecting an increase minus the % expecting a decrease. Source: ANZ Bank

Quarter	Jun-13	Jun-14
Average ordinary time weekly earnings for FTEs (pre-tax) (\$)	\$1,035.12	\$1,062.74
Labour Cost Index - % change in salary and wage rates (including overtime) from the same quarter of the previous year	+1.7	+1.7

Source: Statistics New Zealand.

Household Labour Force Survey	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14
Unemployment Rate (seasonally adjusted, %)	6.4	6.1	6.0	5.9	5.6
Employment Growth (annual, %)*	0.7	2.4	3.0	3.7	3.7

*change since the same quarter of the previous year based on seasonally adjusted data. Source: Statistics New Zealand.

Next Release: *Household Labour Force Survey: September 2014 quarter.* **Date:** 5 November 2014

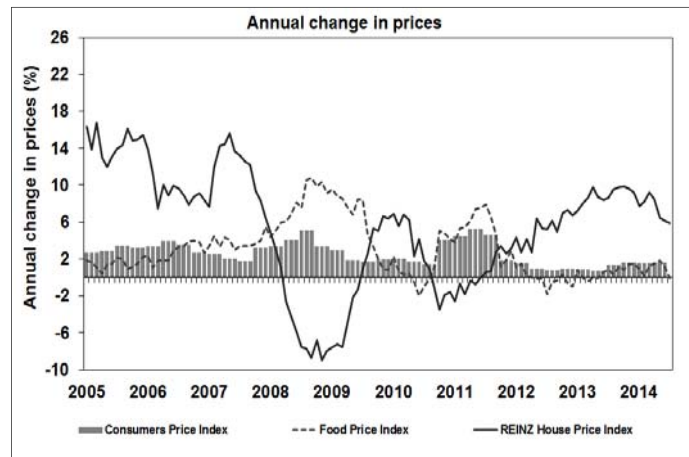
Background

Inflation is the change in prices of goods and services over a certain period of time. The official rate of consumer inflation is measured by Statistics New Zealand's Consumers Price Index (CPI). The CPI tracks the price of a basket of household goods and services over time.

Consumers Price Index

Prices of consumer goods and services rose by 1.6 percent during the year ended in the June 2014 quarter. This is below the Reserve Bank's target midpoint of two percent, and within the medium term inflation target band of 1 – 3 percent.

An increase in the excise duty on tobacco and tobacco products from 1 January was the main driver behind a 10.2 percent price rise in cigarettes and tobacco product prices over the year. Costs associated with the purchase of new housing rose by 4.6 percent during the year (up 6.4 percent in Canterbury and 5.5 percent in Auckland), while housing rental costs rose by 2.2 percent (up 5.2 percent in Canterbury). Household electricity prices rose by 4.5 percent over the year to June 2014.



Inflation of 0.3 percent in the June 2014 quarter was influenced by higher seasonal vegetable prices (up 13.3 percent), and electricity costs (up 4.2 percent). Package holiday costs fell by 6.5 percent over the quarter, while the cost of fruit fell by 4.9 percent.

Other data

Quotable Value has reported that average residential property prices rose by 6.4 percent in the year ended September 2014, with prices rising by 1.1 percent over the last quarter. The average residential property price in September was \$481,497 nationally, and \$731,302 in the Auckland region.

NZIER's latest *Quarterly Survey of Business Opinion* reported that "past capacity pressures are lifting costs, prices and margins". A net 21 percent of responding firms were expecting costs to increase in the upcoming quarter, while a net 29 percent of firms are expected to raise prices (both of these results were below their long-term averages).

Annual Percentage Change (%)	Aug-14	Sep-14
Quotable Value – Residential property values*	6.9	6.4
REINZ Stratified Median Housing Price Index**	4.8	n/a
Food Price Index**	0.7	n/a

*change since the same three months ended in the month of the previous year

**change since the same month of the previous year. Sources: Quotable Value; REINZ; Statistics New Zealand

ANZ Business Outlook Survey	Aug-14	Sep-14
Net % of respondents expecting to increase prices in 3 months' time*	23.2	19.2
Inflation expected in 12 months' time	2.51	2.46

*equal to the % of respondents expecting an increase minus the % expecting a decrease. Source: ANZ Bank.

Outlook

The Reserve Bank in its September *Monetary Policy Statement* has forecast annual inflation to remain under two percent until the September 2016 quarter. Tradables inflation is expected to rise over the medium term with a forecast depreciation in the New Zealand dollar. A gradual rise in non-tradables inflation has also been forecast. *NZIER Consensus Forecasts* has the annual inflation rate rising to 2.3 percent in 2016/17.

Inflation (%)	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14
Consumers Price Index - Annual	0.7	1.4	1.6	1.5	1.6
Tradables inflation	-1.6	-0.5	-0.3	-0.6	0.1
Non-tradables inflation	2.5	2.8	2.9	3.0	2.7
CPI - quarterly	0.2	0.9	0.1	0.3	0.3

Source: Statistics New Zealand.

Next Release: Consumers Price Index: September 2014 quarter.

Date: 23 October 2014

Background

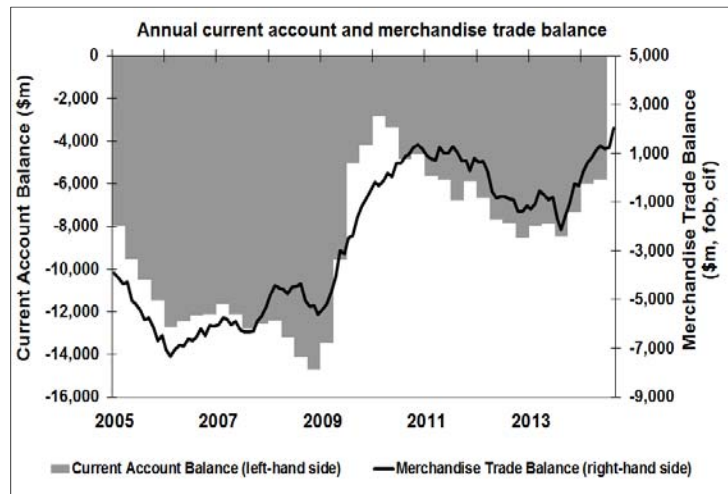
The balance of payments is the record of the receipts and payments between a country's residents and the rest of the world, over a given period. The current account is that part of a country's balance of payments which embraces its transactions of goods, services, primary income (i.e. international income), and secondary income (i.e. current transfers such as foreign aid). A "balance of payments deficit" refers to a deficit of the current account.

Current account deficit

The current account deficit for the June 2014 quarter was \$1,983 million (in seasonally adjusted terms). During the quarter, goods exports fell by \$1,102 million, due to falls for a number of commodity groups (especially for dairy product exports).

On an annual basis, New Zealand's current account deficit totalled \$5,798 million in the June 2014 year, equivalent to 2.5 percent of GDP. This compares with a deficit equivalent to 3.7 percent of GDP a year earlier.

The net international investment position, which shows the net amount we owe the rest of the world, totalled \$149,681 million at 30 June 2014, which was equivalent to 65.3 percent of GDP (the lowest proportion of GDP in almost 13 years).



Other data

Global dairy prices fell by a further 7.3 percent in early October, and are now 48 percent lower than they were in February. The latest ANZ *Commodity Price Index* fell by a further 1.3 percent in September, with dairy product prices leading the decline. However, three commodities recorded an increase in prices, with beef prices reaching their highest level since the index commenced.

Annual Change (%)	Aug-14	Sep-14
World Commodities Prices*	-7.2	-9.4
NZ\$ Commodities Prices*	-12.5	-9.9
Overseas Visitors**	5.3	n/a

*change since the same month of the previous year. **change since the previous year-end. Sources: Statistics New Zealand; ANZ.

Outlook

The ANZ, ASB and Westpac banks expect the current account deficit to remain low in 2014, but to rise as a result of falling terms of trade especially due to lower international dairy prices. The ANZ Bank expects "...sedate rates of consumption growth going forward...", while the ASB Bank believes that "...domestic demand will remain firm..." resulting in greater import demand. Westpac Bank expects the deficit to peak at around five percent of GDP by June 2015.

Balances (\$m)	Jun-13	Sep-13	Dec-13	Mar-14	Jun-14	Aug-14
Quarterly Current Account (seasonally adjusted)	-2,108	-2,428	-851	-617	-1,983	n/a
Annual Current Account	-7,893	-8,475	-7,349	-6,004	-5,798	n/a
Goods	205	-363	1,207	2,680	3,220	n/a
Services	1,056	1,045	1,075	1,268	1,377	n/a
Primary income (i.e. investment income)	-8,670	-8,679	-9,200	-9,517	-9,971	n/a
Secondary income (i.e. current transfers)	-484	-478	-430	-435	-424	n/a
Net international investment position (as at date)	-149,726	-147,676	-145,571	-151,048	-149,681	n/a
Annual Merchandise Trade Balance (fob-cif)*	-819	-1,559	-317	798	1,191	2,018

* CIF – Cost of goods imported, including insurance and freight to New Zealand. FOB – Free on board, the value of goods at New Zealand ports before export. Source: Statistics New Zealand.

Next Release: *Balance of Payments: September 2014 quarter.* **Date:** 17 December 2014

Background

The trade weighted index (TWI) is an index of the New Zealand dollar's value against a basket of five overseas currencies, where each currency is weighted by a combination of the size of the associated country's trade with New Zealand (including the Euro group of countries) and their gross domestic product. The official cash rate (OCR) is the interest rate that applies to overnight borrowing and lending between banks and the Reserve Bank. It is currently a key operational feature of monetary policy in New Zealand. The NZX 50 is the main share index of the New Zealand Exchange. It tracks changes in the share prices of the top 50 publicly listed companies by free float market capitalisation on the NZX market. It is a gross index, so it includes the payout of dividends in its calculation.

Recent trends & data

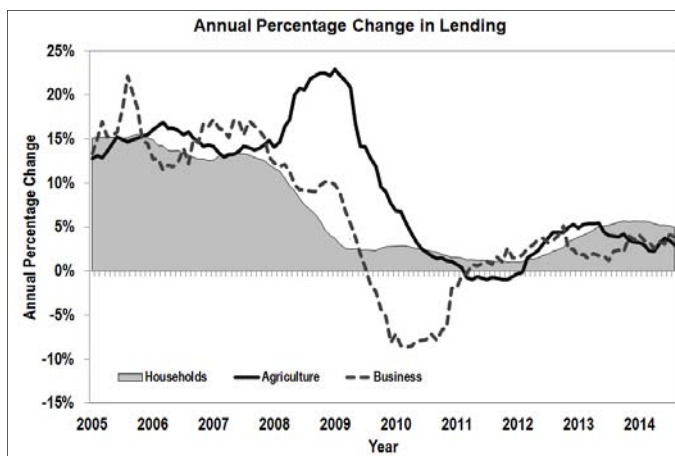
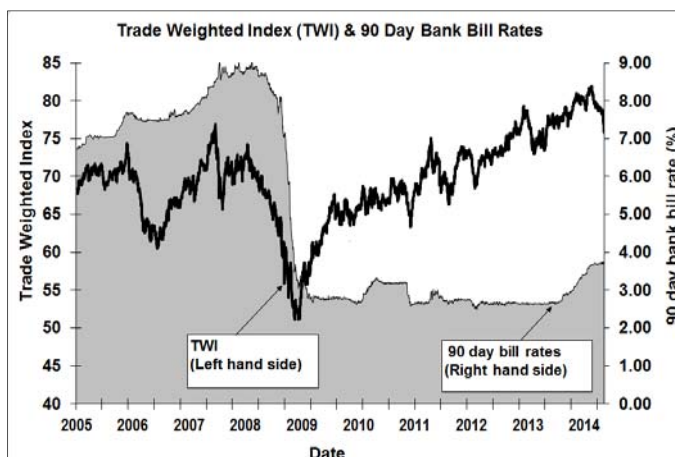
Reserve Bank Governor Graeme Wheeler left the official cash rate unchanged at 3.5 percent in September, following four increases of 25 basis points each earlier in the year. The Governor noted that the economy was adjusting to the tightening of monetary policy to date. Therefore, *"it is prudent to undertake a period of monitoring and assessment before considering further policy adjustment"*.

In a statement released on 25 September, the Governor said that the Bank *"...considers the level of the exchange rate is unjustified and unsustainable, and that it is susceptible to a significant downward adjustment"*. Official figures released later in the month showed that the Bank had intervened in the foreign exchange market in August, selling a net \$521 million into currency markets in order to take the top off the exchange rate. The exchange rate ended September at US77.67 cents, versus US85.28 cents in early August 2014.

High loan-to-value (LVR) lending was equivalent to 6.5 percent of new lending committed in August (after exemptions), according to latest figures released by the Reserve Bank. This compares with high LVR lending accounting for over a quarter of total committed new lending in August 2013.

Outlook

The Reserve Bank in its September *Monetary Policy Statements* has projected the 90-day bank bill rate to peak at 4.75 percent in June 2017, approximately 50 basis points lower than in its June *Monetary Policy Statement*. At this stage, a further 25 basis point increase in the official cash rate is expected around mid-2015.



Core Crown borrowing as at	30-Jun-14 (\$m)	30-Jun-14 (%GDP)
Gross sovereign-issued debt *	81,956	35.8
Net core Crown debt **	59,931	26.2

*Excluding Reserve Bank settlement cash and Reserve Bank bills.

** Excluding NZ Super Fund and other advances. Source: The Treasury.

Monthly averages	May-14	Jun-14	Jul-14	Aug-14	Sep-14
90 Day Bank Bill rate	3.38	3.52	3.67	3.69	3.71
10 Year Government Bond yields (secondary market)	4.29	4.42	4.37	4.20	4.19
Effective mortgage rate	5.73	5.80	5.86	5.94	n/a
Business lending rate	5.68	5.88	5.86	5.94	n/a
Trade Weighted Index (TWI) exchange rate	80.09	80.31	80.93	79.25	78.34
NZX 50 index	5173	5162	5146	5123	5229

Sources: Reserve Bank; NZX.

Next Official Cash Rate (OCR) decision: 30 October 2014

Background

New Zealand's economic growth rate, unemployment rate and central bank interest rates are compared with our main OECD trading partners. The first table below illustrates the seasonally adjusted quarterly growth rates in economic activity. The second table below shows the harmonised unemployment rate in each OECD country/area, while the third shows the main central bank interest rates for various countries (and currency group in the case of the Euro), along with the date and direction of the latest movement for each.

Economic growth

The International Monetary Fund (IMF) has revised down its economic growth forecasts for the advanced economies in 2014 to 1.8 percent. This mainly reflected a lower growth forecast for the United States, from 2.8 percent in the April forecasts to 1.7 percent in the October forecasts. There were also lower economic growth rate forecasts for France in 2014 (0.7 percent versus 1.0 percent) and Italy (0.3 percent versus 0.6 percent). The Chinese economy is forecast to expand by 7.4 percent in 2014 (down slightly from 7.7 percent growth in 2013).

OECD composite leading indicators point towards stable growth momentum for the OECD as a whole, with growth losing momentum in Germany.

Quarterly economic growth rates (%)			
Country*	Dec-13	Mar-14	Jun-14
Australia	0.8	1.1	0.5
Japan	-0.1	1.5	-1.8
NEW ZEALAND	1.0	1.0	0.7
United Kingdom	0.6	0.7	0.9
United States	0.9	-0.5	1.1
Euro area	0.3	0.2	0.0
OECD Total	0.5	0.2	0.4
China	1.7	1.5	2.0

Notes: * Seasonally adjusted growth rate from the previous quarter.
Source: OECD.

Unemployment

In October 2009 the unemployment rates of the United States and the Euro area (which has 18 member countries) were both ten percent. Since then, the United States unemployment rate has fallen to 5.9 percent, while that for the Euro area has risen to 11.5 percent. In July 2014, the harmonised unemployment rate for the OECD area as a whole was 7.4 percent, with New Zealand ranking 9th lowest in the OECD in terms of our unemployment rate.

Harmonised unemployment rates (%)			
Country	Jul-14	Aug14	Sep-14
Australia	6.4	6.1	n/a
Japan	3.8	n/a	n/a
NEW ZEALAND	5.6 (Jun qtr)	n/a	n/a
United Kingdom	6.4 (May)	n/a	n/a
United States	6.2	6.1	5.9
OECD Total	7.4	n/a	n/a

Sources: OECD; Australian Bureau of Statistics.

Central banks

The European Central Bank left its main refinancing rate at 0.05 percent in early October, but provided operational details around its programme of purchasing asset-backed securities and covered bonds. In doing so, the Bank will inject cash into the economy, which will hopefully boost lending and increase economic growth. The programme is to last for at least two years, with asset purchases to commence in the fourth quarter of 2014.

The U.S. Federal Reserve continues to reduce the size of its quantitative easing programme. From October, the Bank will purchase US\$15 billion per month of agency mortgage-backed securities and long-term Treasury securities per month. This compares with an asset purchase programme of US\$85 billion per month at the height of the global financial crisis.

Central Bank interest rates (as at 8 October 2014)				
Central Bank	Key Rate	Interest Rate (%)	Effective from	Direction (Basis points)
Australia	Cash Rate	2.50	7-August-13	-25
China	Benchmark lending rate	6.00	6-Jul-12	-31
European Central Bank	Main Refinance Rate	0.05	10-Sep-14	-10
Japan	Uncollateralized overnight rate	0.00 - 0.10	5-Oct-10	-10
NEW ZEALAND	Official Cash Rate	3.50	24-Jul-14	+25
United Kingdom	Bank Rate	0.50	5-Mar-09	-50
United States	Federal Funds Rate	0.00 - 0.25	16-Dec-08	-75

Source: Central Bank interest rates as at the date stated.

New Zealand Income Survey

Statistics New Zealand produces an annual *New Zealand Income Survey* which is included as a supplement to the *Household Labour Force Survey*. The income survey includes a range of gross (i.e. pre-income tax) income statistics, which are “...used to make policy decisions on economic and social issues...including retirement, education, income tax, minimum wage, and infrastructure developments”. The survey has been undertaken each June quarter since 1997.

The New Zealand Income Survey is a preferred source for providing figures in response to questions such as:

- What is the average weekly or hourly wage?
- What do the self-employed earn?
- What is the distribution of income in New Zealand, by ethnicity, age, sex, or qualifications?
- How much income do people receive by region?
- How much income do people not in paid employment receive?

Results from the June 2014 survey found that:

- For those aged 15 years and over who were earning a wage or salary, the median hourly earnings was \$21.94 per hour. For those working full-time (i.e. 30 or more hours per week), median hourly earnings was \$23.44 per hour, while for those working part-time, median hourly was \$16.96 per hour.
- Average hourly earnings were \$26.78 per hour for those earnings an income from a wage or salary. For a full-time worker, the average hourly earnings were \$27.54 per hour, while average hourly earnings were \$24.30 per hour for a part-time worker.
- The median weekly income from wages or salaries was \$863 per week for those that received a wage or salary. This represented an increase of \$19 per week from the previous year. The average weekly income from wages or salaries was \$991 per week for those that received a wage or salary.
- Median weekly income for all people aged 15 years and over from all sources was \$600 per week, which represented a \$25 per week increase from a year earlier. All sources include income from wages and salaries, self-employment, government transfers, investment earnings, and other transfers.
- The average weekly income from all sources was \$780 per week.
- For all people aged 15 years and over, average weekly earnings were the highest in the Wellington region, at \$901 per week (up \$55 per week from a year earlier). This was followed by the Canterbury and Southland regions, with average weekly earnings of \$808 per week. The Manawatu-Wanganui region had the lowest average weekly earnings, at \$646 per week.
- For those not in paid employment, the median weekly income was \$260 per week. The majority of this amount was received through government transfers. The average weekly income was \$251 per week. Approximately 38 percent of those not in paid employment were aged 65 years and over, with another 15 percent aged between 15 and 19 years.
- Median household income was \$1,422 per week, while average household income was \$1,706 per week.

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